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OAKWOOD

1978

OAKWOOD PETROLEUMS LTD.

Incorporated under the laws of Canada on November 28, 1925 Capital: 7,000,000 shares without nominal or par value, of which 4,778,277 (net) shares are issued and outstanding.

Directors

Dallas E. Hawkins II,
Spokane, Washington, U.S.A.
President of the Company
Chairman of the Board of
American Eagle Petroleums Ltd.

Brian S. Ekstrom,
Calgary, Alberta
Vice-President of the Company
Treasurer of American Eagle
Petroleums Ltd.
President of Brian Ekstrom
Management Ltd.

Kenneth W. Germond,
Calgary, Alberta
Vice-President
of the Company

R. Ross Hamilton,
Calgary, Alberta
President of Great Basins
Petroleum Co.
President of Scoteire
Exploration Ltd.

Richard D. Jensen,
Calgary, Alberta
Executive Vice-President
of the Company

Gerhard Kasdorf,
Calgary, Alberta
Vice-President of the Company
and President of
American Eagle Petroleums Ltd.

Brian G. McCombe,
Calgary, Alberta
Partner, McCombe Cameron

Edward G. McMullan,
Calgary, Alberta
President of E. G. McMullan Ltd.

Jack Wahl,
Calgary, Alberta
Chairman of the Board and
Chief Executive Officer of
Great Basins Petroleum Co.

Officers

Dallas E. Hawkins II,
President

Richard D. Jensen,
Executive Vice-President

Brian S. Ekstrom,
Vice-President, Finance

Kenneth W. Germond,
Vice-President, Exploration

Gerhard Kasdorf,
Vice-President, Production
and Operations

Brian G. McCombe,
Secretary

Head Office

2700 Shell Centre
400 - 4th Avenue S.W.
Calgary, Alberta T2P 0J4

Subsidiary Companies

Marwood Petroleum Ltd.
Bayview Oil & Gas Ltd.
Flamingo Oils Limited (N.P.L.)
Orient Investments Ltd.
Oakwood Petroleum Corporation
Oakwood Petroleums (Ireland) Ltd.
Oakwood Petroleums Italiana S.p.A.
Lochaber Oil Corporation Ltd.
Bueno Oils Ltd.
Coronado Consultants Ltd.
Huron Resources Management Ltd.
American Eagle Petroleums Ltd.
American Eagle Petroleums, Inc.
Gull Oil & Gas Ltd.

Shares Listed

The Toronto Stock Exchange

Bankers

The Royal Bank of Canada
Calgary, Alberta

Continental Illinois National Bank and
Trust Company of Chicago —
Chicago, Illinois and Toronto, Ontario

Auditors

Thorne Riddell & Co.
Calgary, Alberta

Registrar

Canada Trust Company
Calgary, Alberta

Transfer Agents

Canada Trust Company,
Calgary, Alberta
and Toronto, Ontario

HIGHLIGHTS - 1978

PRODUCTION STATISTICS

	1978	1977	1976	1975	1974
Oil Production, Barrels	**450,000**	336,736	204,345	161,182	173,214
Daily average, Barrels	**1,233**	923	560	442	475
Gas Production, MCF	**3,725,000**	3,564,276	1,906,542	1,317,963	1,187,996
Daily average, MCF	**10,205**	9,765	5,223	3,611	3,255
SALES & EARNINGS					
Crude Oil & Natural Gas Sales	**7,409,659**	5,434,977	2,594,838	1,428,553	1,060,939
Funds provided by Operations	**3,651,948**	2,781,958	1,459,830	484,966	269,948
Per Share	**76¢**	60.5¢	33.5¢	13.3¢	7.4¢
Earnings (Loss) for the year	**738,797**	992,693	442,273	(126,596)	(798,172)
Per Share	**15¢**	22¢	10¢	(03¢)	(22¢)
LAND HOLDINGS					
Oil & Gas Lease & Permit Acres					
Gross acres	**9,939,428**	4,011,305	1,265,318	1,042,102	846,776
Net acres	**1,226,981**	413,643	221,048	163,053	116,733
Mining Claims & Exploration					
Gross acres	**9,416**	9,416	66,664	65,898	65,898
Net acres	**787**	787	6,666	6,451	6,451
NET RESERVES					
Oil and Condensate, Barrels					
Proven	**3,637,402**	2,070,000	1,640,000	1,016,000	1,072,000
Probable	**343,010**	1,021,000	695,000	320,000	621,000
TOTAL	**3,980,412**	3,091,000	2,335,000	1,336,000	1,693,000
Natural Gas, MMCF — proven and probable	**151,035**	75,583	44,596	28,490	24,150
Indicated Sandhills Gas Reserves, MMCF (net of royalty)	**103,000**	103,000	103,000	103,000	103,000

ANNUAL MEETING OF SHAREHOLDERS

Annual General Meeting of Shareholders of Oakwood Petroleums Ltd. will be held in the Lake Louise Room of the Calgary Inn in the City of Calgary, Alberta at the hour of 10:00 A.M. Local Time June 28, 1979. A formal Notice of Meeting of Shareholders together with an instrument of Proxy and Information Circular is being mailed to the shareholders concurrently.

PRESIDENT'S REPORT TO THE SHAREHOLDERS

It is a pleasure to present our consolidated Annual Report for the year just ended. As predicted in the 1977 Annual Report and to the shareholders' meeting last June, continuously increasing cash flows have enabled Oakwood's management to consider and complete a number of highly ambitious programs. While the full impact of these efforts are not fully reflected in this year's financial review, we are delighted with our 1978 accomplishments.

Measured in terms of producing assets, your Company now owns net reserves of 3,980,000 bbls. of oil and liquid hydrocarbons, and over 151 billion cubic feet of gas. This growth in our reserve base, up from 3,091,000 bbls. of oil and liquid hydrocarbons and 75 billion cubic feet of gas reported last year, was affected by a combination of selective producing asset acquisitions and the impact of our first-ever drilling program.

Measured in terms of cash flow, 1978 reached a new all time high of $3,652,000 or 76¢ per share, up 31% from the previous record level attained in 1977. This continuing growth in your Company's cash flow should be sustained through 1979 and beyond, thus enabling further enhancement of reserves through additional acquisitions, and drilling activity.

Measured in terms of net earnings, 1978 was a disappointment. Although revenues increased, the impact of high interest charges and deferred income taxes (taxes not paid but provided for) reduced earnings to $739,000 or 15¢ per share. While the earnings are down from those reported in 1977, we look upon 1978 as a milestone in the growth and development of Oakwood. It is important to note that many of the 1978 achievements occurred late in the year and consequently had little impact on our earnings position.

Of particular significance, 1978 saw your Company acquire assets for an aggregate price of $37,000,000. These assets, largely producing oil and gas properties, were almost entirely purchased with the help of self-liquidating loans. Our present debt position, as indicated in the financial section, is of course, more than offset by the value of purchased assets. It is noteworthy that Oakwood virtually doubled its oil and gas reserves during 1978.

In the course of acquiring these new reserves your Company was fortunate in also adding valuable exploration lands to its acreage inventory. These important additions have established the essential ingredients for a sustained and serious exploration effort. Our land position of 1.2 million net acres has enabled Oakwood to structure and obtain commitments for a $4,000,000 exploration drilling partnership for use during 1979. When formally registered, this program will be in addition to the development drilling now in progress which is exploiting our highly successful 1978 exploration effort.

Added to our domestic exploration and development activity, we have continued to drill and evaluate our Freestone County, Texas, land where we now enjoy an interest in ten deep gas wells. Although gas markets have been slow in coming, a number of the wells have commenced gas delivery under a contract with United Texas Transmission Co. Additional development is contemplated, and indeed two wells are currently drilling in this highly prospective area.

Other international activity is progressing satisfactorily with seismic activity either in progress or just completed in Australia and the Seychelles Islands. Extensive evaluation of this geophysical data will, of course, be required before drilling can be contemplated.

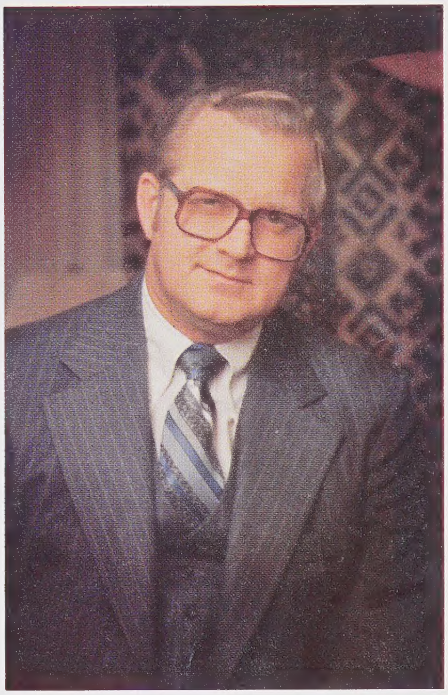
Turning to the future, we fully intend to maintain a growth posture. Our optimism is based on our belief in expansion of gas markets and improving crude oil and natural gas prices.

Our pricing expectations are framed in the context of international energy shortages which are clearly beginning to emerge on many fronts. With these shortages, we find the federal pricing constraints and consumer subsidies out of harmony with any serious attempts to implement national voluntary energy conservation measures. Moreover, we view artificially suppressed petroleum prices as a major impediment to the development of alternative energy forms which will inevitably be required to satisfy our national energy appetite. Evidence of mid-East unrest and the certainty of future OPEC price escalations would seem to dictate immediate public acceptance of high energy prices in both Canada and the U.S. From Oakwood's viewpoint, the pricing imponderables imposed by forces other than supply and demand, frequently represent the most hazardous ingredient in our exploration and development decision process. These decisions must, of course be aggressively made if Canada is to have an assured source of petroleum energy for the future.

While there are some concerns, we regard some of these as an opportunity for further growth and development. We are, therefore, grateful for a dedicated staff and their continued support. We also wish to express our gratitude to our shareholders for their confidence, both in Oakwood and the future.

Dallas E. Hawkins II

Dallas E. Hawkins II
President



Richard D. Jensen — Executive Vice President

EXPLORATION & LAND

Involvement in meaningful exploration was one of the Company's prime objectives during 1978. Additional geological and land staff were employed, and Oakwood's first exploratory drilling program was created and set in motion with sufficient drillable prospects to make it a success. It is anticipated that further staff additions will be made in 1979 so that the Company can properly operate its second and third drilling programs as well as carry out routine exploration and development duties.

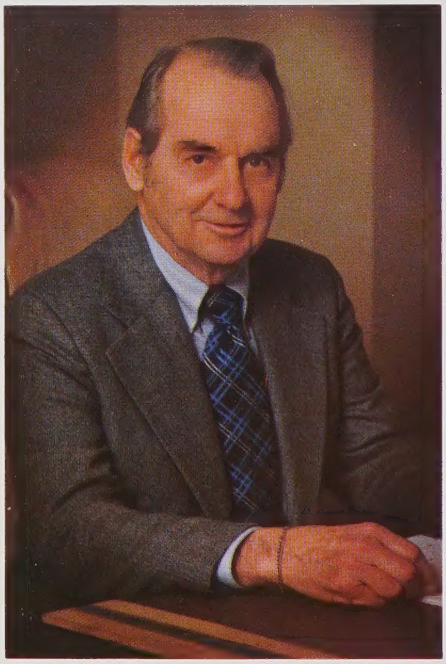
Alberta and British Columbia comprised the scene for most of our exploratory activity during 1978. Eighteen wells had been drilled or spudded by year's end, twelve of which were the result of farmins; this program resulted in the discovery of two oil fields and six gas fields. Two seismic programs were participated in and several similar studies were evaluated. Activities by the industry in the vicinity of Oakwood's ever increasing lease position were under close scrutiny and several worthwhile plays are being considered for the immediate future.

Development drilling in and around the Company's existing producing fields was rewarding in that several gas contracts were kept at or near maximum capacity. Fields capable of producing additional oil were closely studied for expansion possibilities. The year 1979 should see a significant increase in the drilling of development wells for oil as the new discoveries are exploited.

LAND ACTIVITIES

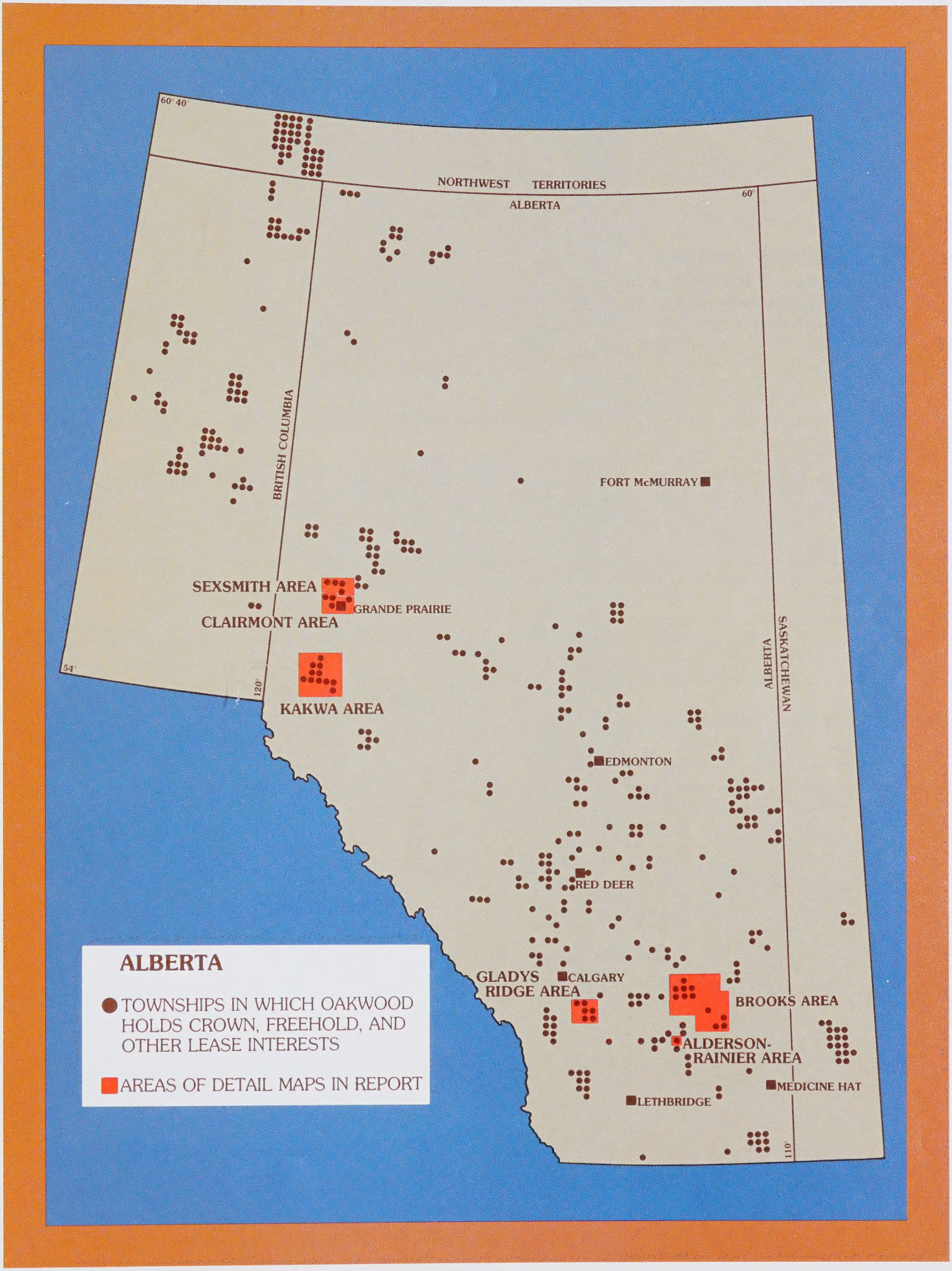
Increasing the Company's land holdings was given high priority during the year, resulting in substantial improvements in this particular asset category. Acquisition of the land inventories held by the companies whose assets were purchased during the year provided many valuable leases, most at a lower price than available through normal competitive channels. Lease acquisition from the government by sealed tender has become very expensive and competitive, thus adding to the importance of having in hand an attractively priced lease inventory upon which to base exploratory drilling.

Other lease interests were acquired via the farmin route, utilizing the Company's leased drilling rigs and the exploratory drilling programs to earn various working interests under anomalous lands. In Australia, two large exploration permits were negotiated for minimal work commitments.



Kenneth W. Germond — Vice President - Exploration

As a consequence of these various operations, the gross acreage position of the Company and its subsidiaries increased 250%, while the net acreage count improved 300%. Activity in early 1979 continues to be aggressive in several highly potential areas of Alberta and British Columbia.

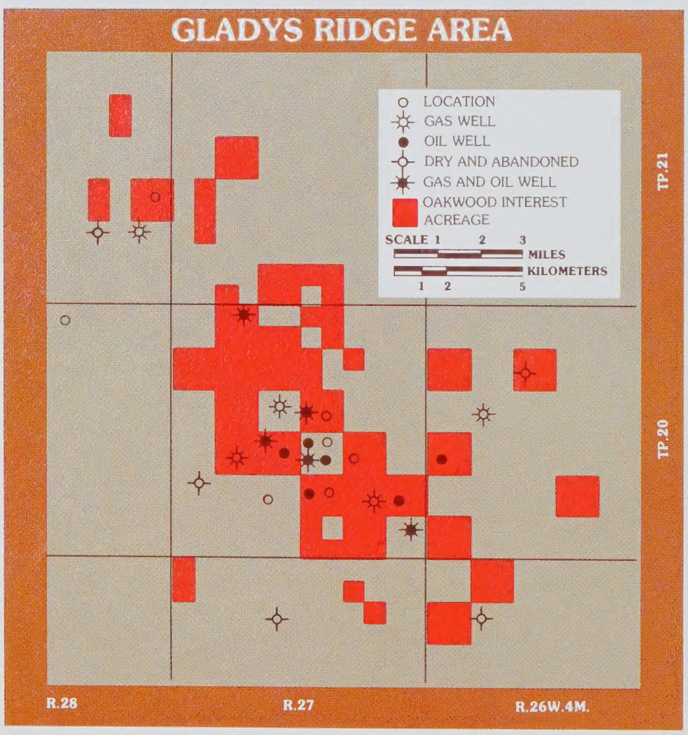

60° 40'
NORTHWEST TERRITORIES
ALBERTA
60°
BRITISH COLUMBIA
FORT McMURRAY
SEXSMITH AREA
GRANDE PRAIRIE
CLAIRMONT AREA
54°
120°
KAKWA AREA
ALBERTA
SASKATCHEWAN
EDMONTON
RED DEER
GLADYS RIDGE AREA
CALGARY
BROOKS AREA
ALDERSON-RAINIER AREA
MEDICINE HAT
LETHBRIDGE
110°
ALBERTA
TOWNSHIPS IN WHICH OAKWOOD HOLDS CROWN, FREEHOLD, AND OTHER LEASE INTERESTS
AREAS OF DETAIL MAPS IN REPORT

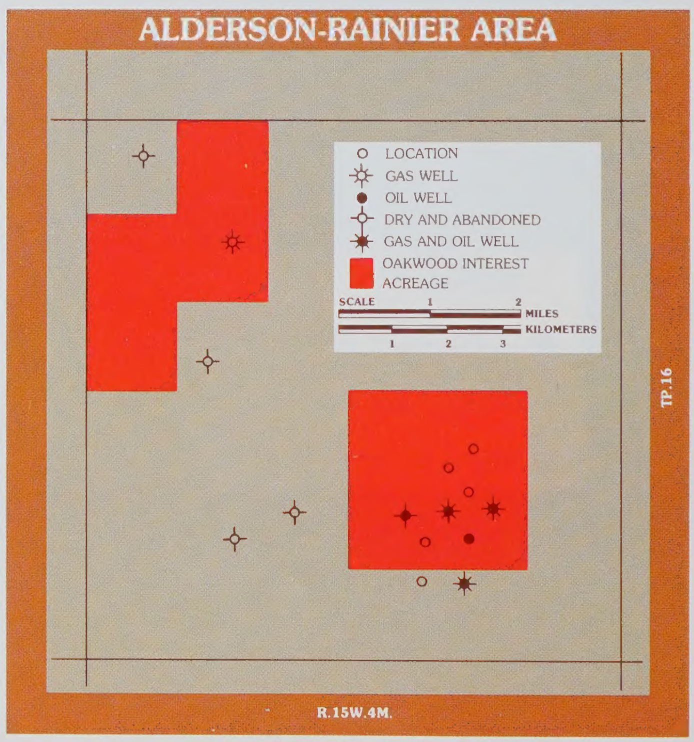
OAKWOOD PETROLEUMS LTD., AMERICAN EAGLE PETROLEUMS LTD., AND SUBSIDIARIES, OIL AND GAS RIGHTS HELD AT JANUARY 1, 1979

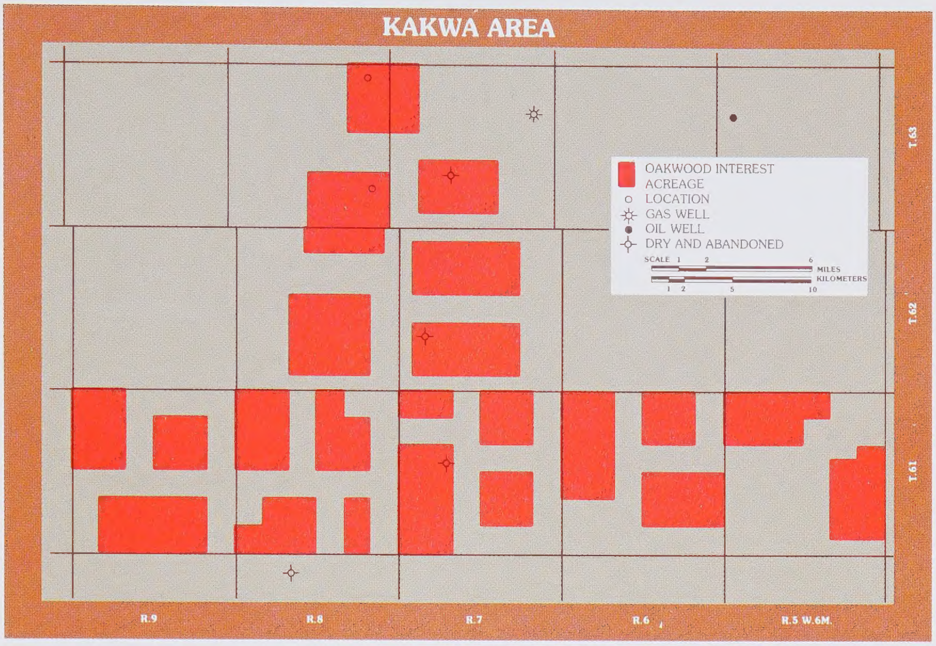
	Gross	Net
WESTERN CANADA		
Alberta	1,460,080	157,082
Saskatchewan	286,992	70,792
Manitoba	640	60
British Columbia	223,689	23,925
NORTHERN CANADA		
Northwest Territories	756,350	128,124
Yukon	37,696	1,571
EASTERN CANADA		
Ontario	7,396	2,980
Offshore Labrador	753,404	36,492
Offshore Newfoundland	430,284	*

	Gross	Net
UNITED STATES		
Montana	87,468	6,972
North Dakota	743	556
Ohio	761	559
Texas	26,352	2,927
Kentucky	15,130	*
California	1,108	607
Kansas	5,420	339
FOREIGN		
German North Sea	98,842	2,111
Seychelles Islands	847,073	105,884
Western Australia	4,900,000	686,000
	9,939,428	1,226,981
Mining Claims	9,416	787

*Overriding Royalty Interest Only





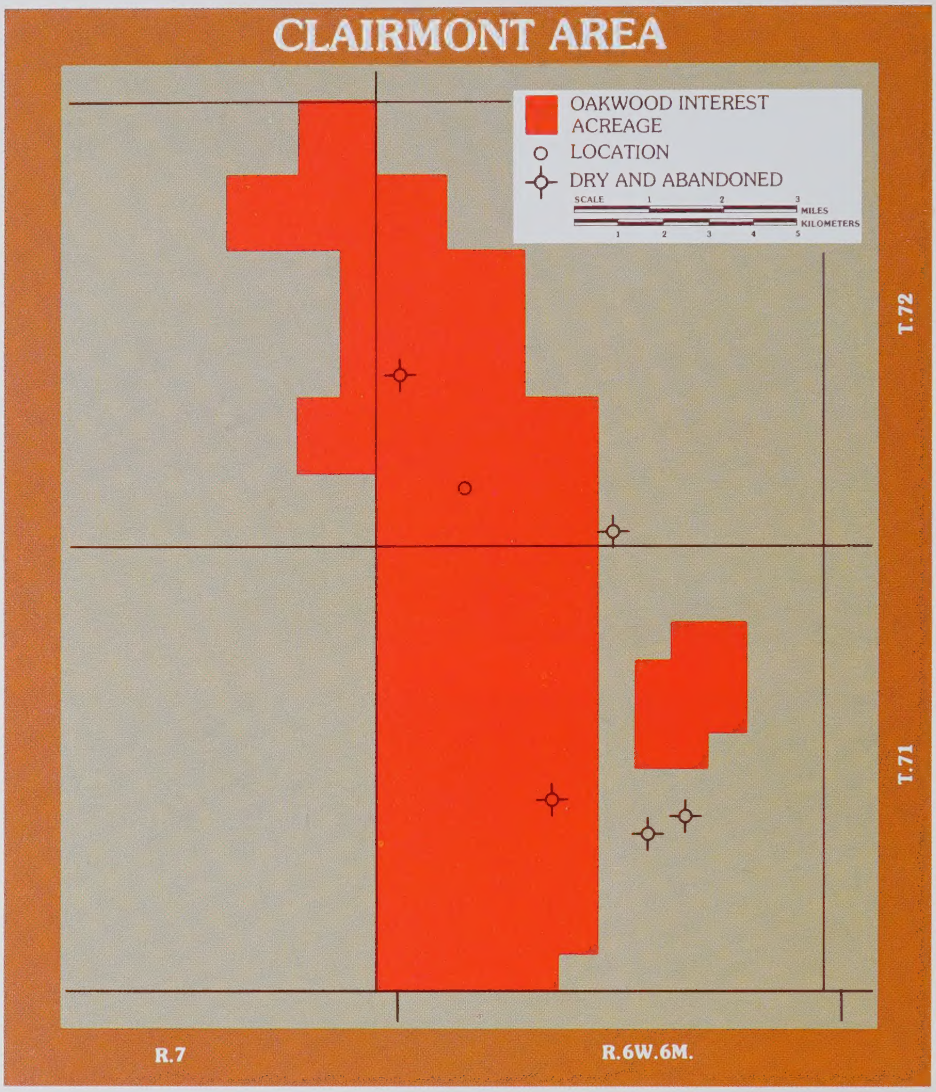


GLADYS RIDGE AREA

Oakwood has a substantial lease position in the rapidly expanding multi-pay oil and gas Gladys Field, 25 miles south of Calgary. Drilling in the field was stimulated in 1977 with the discovery of Mississippian oil from the Elkton formation and oil and gas from the overlying Cretaceous Basal Quartz sands. These, added to the earlier discoveries of gas in the Devonian Crossfield zone and from the shallow Cretaceous Belly River sands, have caused nine wells to be drilled in 1978 with six further tests contemplated for early 1979. Feasibility studies as to the construction of a gas plant for the processing of the gas reserves are soon to be completed. Oil from the Basal Quartz and the Elkton is being trucked to market pending the construction of a pipeline.

ALDERSON — RAINIER AREA

Two of the discoveries made in 1978 under the Oakwood Exploration Drilling Program were located in the Alderson area of Southeastern Alberta. The Rainier 10-29 well encountered gas in the Cretaceous Glauconitic sand and is shut-in, waiting on a gas contract. Oakwood earned a 25% interest in the well and under three sections of adjoining leases. To the southeast and in the same township, Oakwood teamed with two partners to drill a Glauconitic sand oilwell discovery at Alderson 6-11. Subsequently, the team drilled two offsets, each of which indicated oil in at least one zone plus gas from the overlying Cretaceous Viking sand. Oil production has commenced and further development at six other offsets will be carried out in early 1979. Oakwood has a $12^{1}/_{2}$% interest in the four section lease block around the discoveries.



KAKWA AREA

Oakwood is modestly involved in the Steep Creek-Elmsworth-Kelly Lake exploratory trend of Western Alberta - Eastern British Columbia. The Kakwa area, 40 miles south of the Elmsworth area of concentration, has several active rigs exploring the deep prospective Cretaceous horizons producing to the north and the east. The Company's lease position is comprised of 3,138 net acres under 89,168 gross acres; one wildcat well on one of the leases was drilled to 3,418 metres (11,214 feet) total depth and abandoned in March 1979 for lack of economic gas showings. Another similar well located four miles north has been approved for drilling in mid-1979. Forty miles to the southeast, Oakwood has lease interests of 1,555 net acres under 50,907 gross acres located on the Forest trend. And in British Columbia, at Kelly Lake, the Company has a 1,282 acre lease interest under 15,388 gross acres situated at the west extension of the Elmsworth field. It is anticipated that the Company will participate in further drilling along this active, promising trend for the next several years.

CLAIRMONT AREA

Oakwood has varying lease interests under 23,360 gross acres immediately west of the town of Grande Prairie, Alberta. This acreage is situated just four to six miles east of several reliably reported Triassic oil and gas discoveries that were completing at year's end. Industry interest in the immediate area between the discoveries and the lease blocks in which Oakwood is involved is such that 36,320 acres of unleased Crown acreage was posted for sale in March and April 1979. These sales realized the province in excess of $41,700,000 for an average of approximately $1,100 per acre. Oakwood is participating in the drilling of a 3,709 metre (12,185 feet) exploratory well in the middle of its block.

SEXSMITH AREA

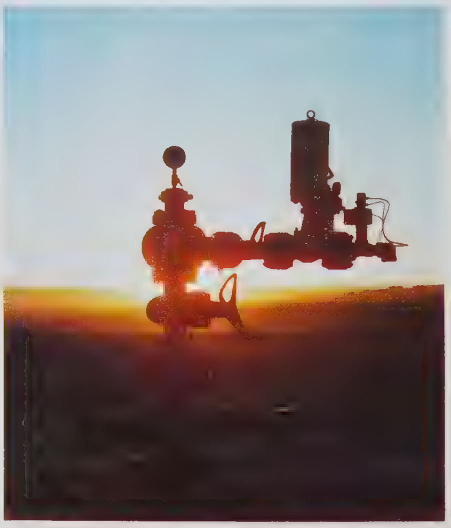
At Sexsmith, seven to ten miles north of the Clairmont block, Oakwood has nominal lease interests under 18,500 acres. Six sections, or 3,840 acres, is considered proven for gas in several Cretaceous sands as well as the Triassic and the Permian. Production should commence as soon as gas contracts are available. The unproven acreage is prospective in those horizons in which the new discoveries located to the southwest have been completed.

EAST TEXAS JURASSIC TREND

Exploratory drilling for the deep Jurassic gas production continued throughout the year. The Company has participated in ten operations, all of which are indicated as successful ventures. Gas reserves have been established in three different zones in the Jurassic and one in the overlying Cretaceous. At year end, three of the wells were producing on a restricted basis and seven were being readied for gas delivery.

There has been an unavoidable delay in delivery of gas to interstate markets. The local gas gathering systems were filled to capacity and we were obliged to wait for both market expansion and resolution of an uncertain gas pricing situation. Fortunately, in January of this year, the Company and its partners negotiated an acceptable gas sales contract with United Texas Transmission Co.

Because of the market delay, the Company deemed it prudent to reduce its investment exposure in this deep Jurassic trend. Two partners were brought into the program, on a promoted basis, thus reducing Oakwood's position to one half of its original working interest.



Our expectations and development plans for this play have not been altered and, with the establishment of a satisfactory market for the gas production, drilling will be accelerated. During 1979, it is anticipated that Oakwood and its partners will participate in the drilling of at least six or eight additional deep wells, most of which will be evaluation stepouts to the previously completed gas producers.

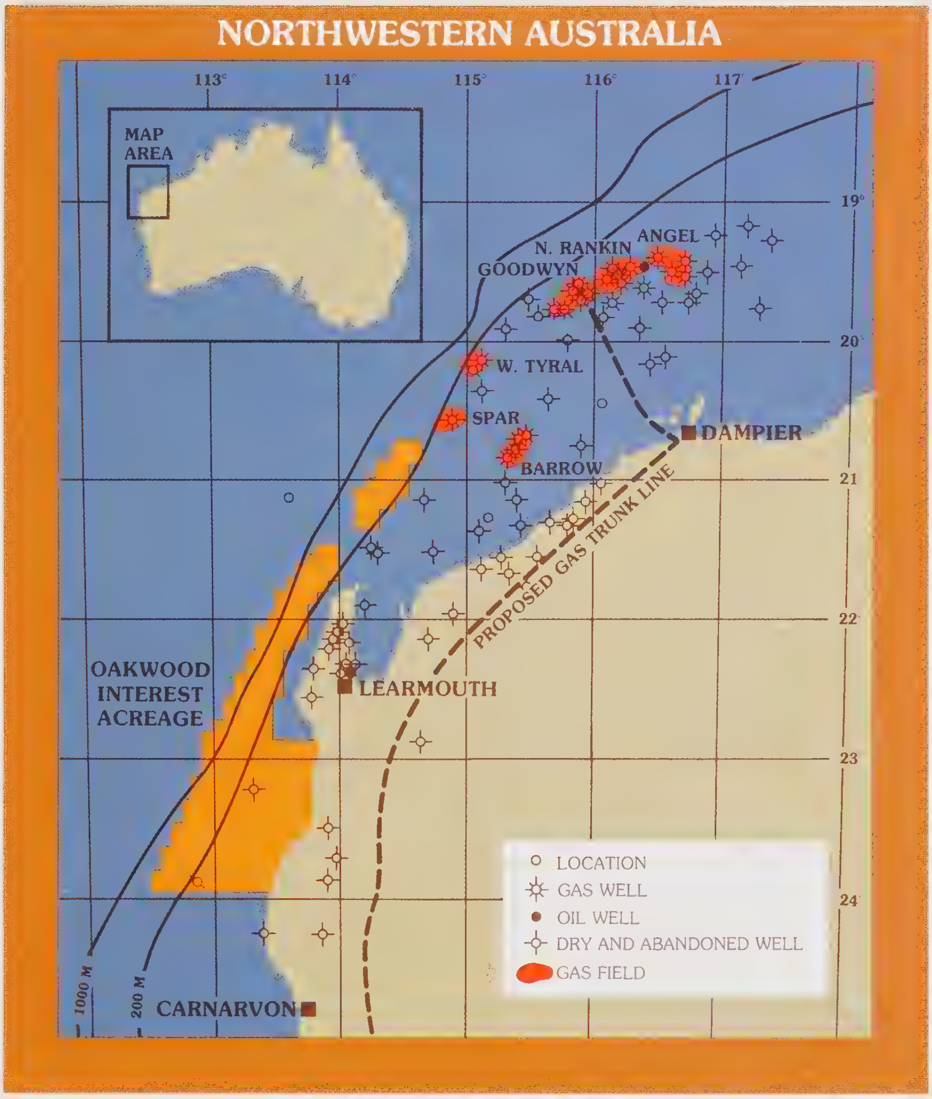
AUSTRALIA

At the end of 1977, the Company and its three partners had undertaken to explore a 4,500,000 acre offshore petroleum exploration permit within the attractive Carnavon Basin, Northwestern Australia. During 1978, the group added to its acreage position with another permit comprising 400,000 acres. This new property lies 24 kilometres to the northeast and on trend with the original permit. The addition was timely and the planned comprehensive marine seismic survey was expanded to cover the overall holdings and vital control points within the area.

Future exploration plans for the offshore permits provide for 400 kilometres of additional infill seismic data, such work to be carried out when a marine crew is available. Because of the shortage of recording vessels, an extension of the work period has been received, allowing for sufficient time to properly process and integrate the new data before proceeding into work periods requiring drilling commitments.

SEYCHELLES ISLANDS

Data from the 400 kilometres marine seismic survey shot in early 1978 was encouraging. Several anomalous structures were evident and also the shallow banks were underlain by what is interpreted to be a normal sequence of sedimentary rocks. Additional infill seismic control is needed and will be acquired in 1979. The drilling commitment date as set by the Government has been set back to allow for the acquisition and interpretation of the additional data.



PRODUCTION AND OPERATIONS

During 1978 your Company increased its oil reserves by 29% and its gas reserves by 178%. This dramatic increase in reserves was the result of an aggressive acquisition effort and drilling program. Oakwood Petroleums Ltd. and its wholly owned subsidiaries participated in the drilling of 78 wells of which 10 were oil, 51 gas and 17 dry. In addition to the above program, American Eagle Petroleums Ltd. (44.2% owned by Oakwood Petroleums Ltd.) participated in the drilling of 34 wells, of which 11 were oil, 16 were gas and 7 were dry. The combined success ratio was approximately 79%.

Three major acquisitions were made during 1978. These were the Canadian assets of Shenandoah Oil Corporation, November 1, 1978; Chief Seneca Oil & Gas Ltd., July 1, 1978; and the Hanover Petroleum Corporation, effective July 1, 1978. As a result of the Shenandoah acquisition, Oakwood acquired an interest in 57 producing wells of which 35 are located in the Verger area and are now being operated by Oakwood Petroleums Ltd. The acquisition of the Shenadoah-Verger properties increased Oakwood's operated wells in the Brooks area to 191.

As a consequence of Oakwood's successful drilling program and production acquisitions in 1978, our year end daily oil production rate was 1,367 bbls. and our gas production had increased to 21.1 million cubic feet per day. Since the major assets were acquired during the latter part of 1978, the annual average figures as shown in our statistics section do not fully reflect the impact of these increased production rates. We can, however, anticipate a significant increase in production during 1979.

With the purchase of the Verger wells, Oakwood acquired a permanent staff of five employees. Oakwood now has sufficient operations in

the Brooks area to warrant a field office, and we have plans to open one in June of this year.

The Company also has contract operators handling properties at Matziwin and Princess. With the opening of the office at Brooks, it is our intention to phase out our contract operators in favor of Oakwood personnel. After the phasing out has been completed, our staff in Brooks will aggregate approximately twelve employees. With this increased field complement, it has also been necessary to expand our Operations Department in Calgary. The current Calgary Operations Group numbers six and will probably be increased to eight by the end of 1979.

Increased drilling activity in Western Canada is creating an almost unprecedented demand for drilling equipment and it is nearly impossible to contract the services of a drilling rig. Fortunately this situation was anticipated by your Company and Oakwood has obtained the services of three drilling rigs under long term contracts. These drilling rigs will allow Oakwood to carry out its scheduled 1979 development operations and simultaneously maintain an active exploratory program.

One of the major areas of concern within the oil industry has been the lack of markets for gas. During 1978 your Company has actively supported Pan Alberta Gas Ltd. in its efforts to obtain additional gas markets. We have also contracted our shut-in reserves to Pan Alberta. Eventual sales are, of course, conditional upon additional gas export approvals. It is gratifying to note that the Alberta E.R.C.B. has recognized an Alberta surplus and has approved gas removal from the province. These approved volumes must now await a decision from the National Energy Board who will rule on any exports from Canada.

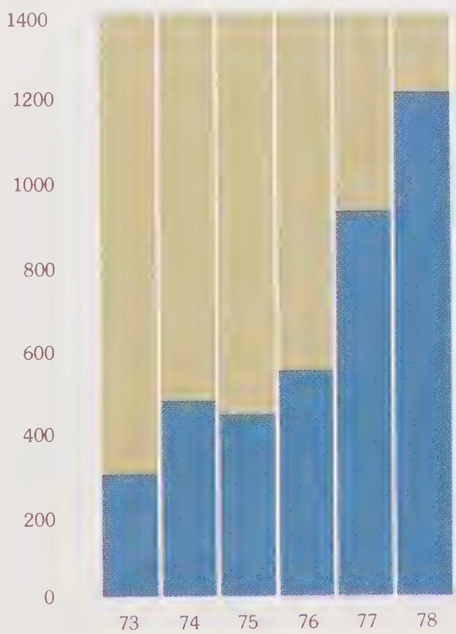
Gerhard Kasdorf — Vice President - Production and Operations.

SHENANDOAH OIL CORPORATION PURCHASE

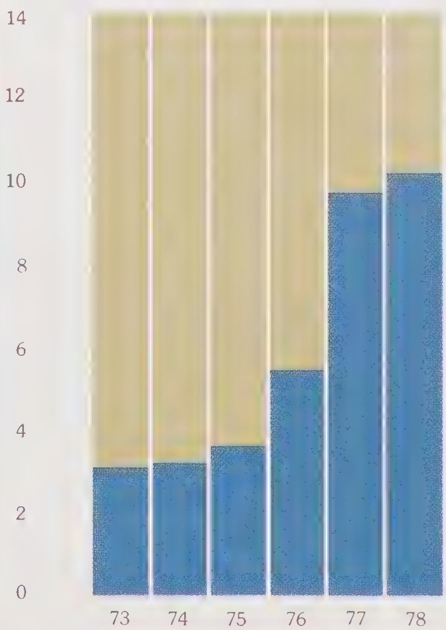
Effective November 1, 1978, Oakwood Petroleums Ltd., together with Norcen Energy Resources Limited and Prairie Oil Royalties Company Ltd., purchased the Canadian assets of Shenandoah Oil Corporation for $47,300,000 of which Oakwood's interest was 50%. The acquisition included various interests in oil and gas properties located in British Columbia, Alberta, Saskatchewan and Ontario. The major producing properties were in Verger and Netook, Alberta, Fireweed, YoYo and Jeans in British Columbia. The operations of the properties were split between Oakwood and Norcen with Oakwood operating the wells in the Verger area.

The Verger property is represented by an interest in 35 producing gas wells and two gas plants. The Fireweed and Jeans areas in British Columbia are represented by 10 gas wells. In the Netook area, Oakwood and partners acquired an interest in two gas wells and a gas plant. In addition to these properties, the acquisition also resulted in a major addition to our exploratory land holdings.

OIL, LIQUIDS
AVERAGE DAILY PRODUCTION
(IN BBLS.)



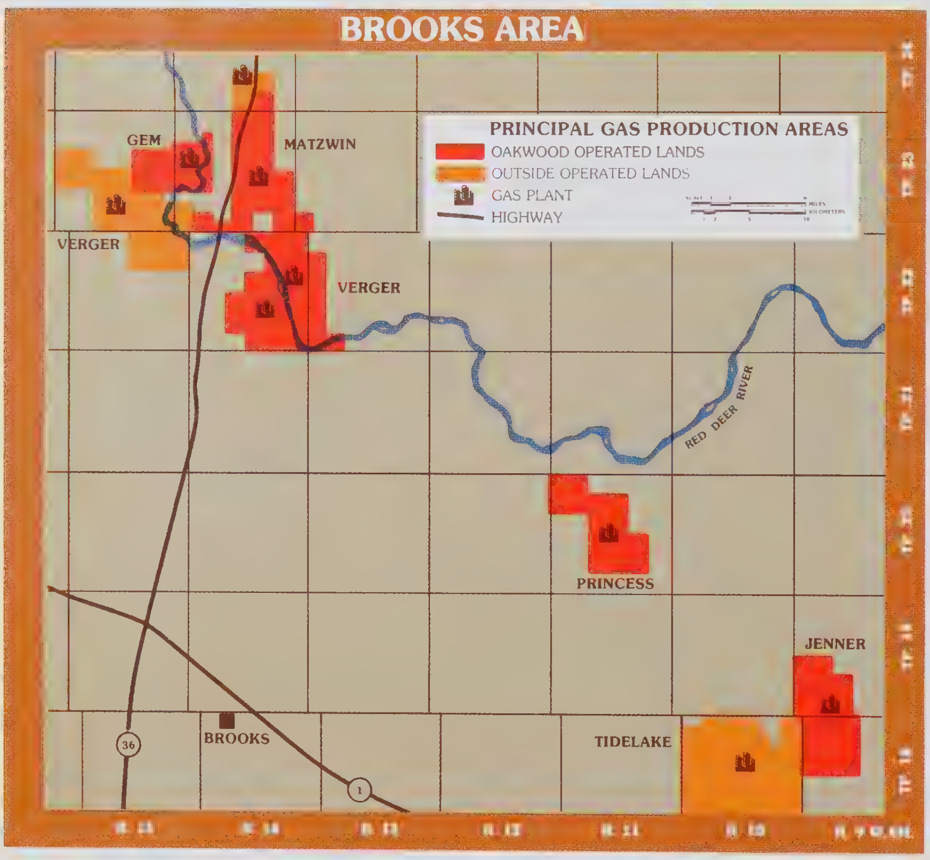
NATURAL GAS
AVERAGE DAILY PRODUCTION
(IN MILLIONS OF CUBIC FEET)



CRUDE OIL & NATURAL GAS
RESERVE SUMMARY as at December 31, 1978

	Working Interest		Net	
	Crude Oil & Liquids	Natural Gas	Crude Oil & Liquids	Natural Gas
	BBLS	MCF	BBLS	MCF
PROVEN RESERVES				
Oakwood Petroleums Ltd. & Subsidiaries	4,675,024	170,275,031	2,981,998	124,648,618
American Eagle Petroleums Ltd.	830,856	29,408,646	655,404	19,163,259
Total Proven Reserves	5,505,880	199,683,677	3,637,402	143,811,877
PROBABLE ADDITIONAL RESERVES				
Oakwood Petroleums Ltd. & Subsidiaries	91,311	4,631,056*	68,272	3,329,519
American Eagle Petroleums Ltd.	421,201	6,176,098	274,738	3,893,604
Total Probable Additional Reserves	512,512	10,807,124	343,010	7,223,123
PROVEN AND PROBABLE ADDITIONAL RESERVES				
Oakwood Petroleums Ltd. & Subsidiaries	4,766,335	174,906,087*	3,050,270	127,978,137
American Eagle Petroleums Ltd.	1,252,057	35,584,744	930,142	23,056,863
Consolidated Proven and Probable Additional Reserves	6,018,392	210,490,831	3,980,412	151,035,000
Metric Volume (cubic meters)	961,740	5,964,600	636,070	4,279,820

*Does not include 103,000 MMCF gas reserves attributed to Sandhills, Saskatchewan property.



CHIEF SENECA OIL & GAS LTD.

Effective July 1, 1978, Oakwood Petroleums Ltd. acquired all of the Canadian producing and non-producing properties from Chief Seneca Oil & Gas Ltd. The major oil producing interest is a 10.295% working interest in the Meekwap D-2 unit. Among other interests are oil producing properties in Drumheller, Suffield, and Lloydminster. Major gas reserves were acquired in the Prophet River, Moose Lick areas of British Columbia along with the Calling Lake, Daysland, Stoddart and Sunlite-Benton areas of Alberta. The properties were acquired for a net total consideration of $8,550,000, and will result in a substantial increase in Oakwood's oil and gas producing rates during the coming years.

HANOVER PETROLEUM CORPORATION

The Hanover Petroleum Corporation asset purchase completed in late December, 1978 but with an effective date of July 1, 1978 was a significant contributor to Oakwood's reserve growth last year. These producing assets, virtually all joint ventures with Chief Seneca, were obtained in a complex two-stage purchase for an aggregate consideration of $2,860,000. In similarity to the Chief Seneca acquisition, the major asset was an interest in the Meekwap D2-Unit. Other important properties included interests in Drumheller, Stoddart and Sundre.

The 1978 asset purchases are reflected in the accompanying tabulation of reserves as prepared by a well known engineering firm.

FINANCIAL REVIEW

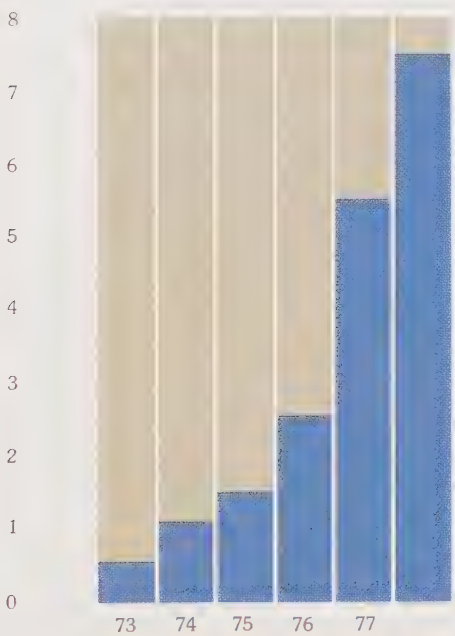
Brian S. Ekstrom — Vice-President - Finance

As mentioned in other areas of this report, 1978 marked another year of unprecedented activity for your Company. Net oil and gas sales increased to $7.4 million in 1978, being up approximately 36% from 1977. Cash flow derived from operations amounted to $3.65 million, an increase of 31% from the previous year. While these indicators give some measure of the Company's continuing growth, they do not give full impact to our present level of operations. 1978 saw the Company continuing its policy of acquiring producing oil and gas properties primarily in Western Canada, committing to purchase in excess of $37,000,000 worth of producing oil and gas assets. As indicated in the accompanying financial statements, $18,000,000 of these acquisition commitments were fully expended in the latter part of 1978, with the balance of $19,000,000 having been expended to consummate the purchases in early 1979. Inasmuch as these acquisitions were not concluded until the latter part of 1978, sales and cash flow levels really did not reflect very much of the ultimate benefits to be derived by the Company from these acquisitions.

These acquisitions were funded primarily by way of additional borrowings from the Company's banks and from secondary lenders. During the year the Company finalized the issuance of $18,000,000 in income debentures, thus serving to reduce significantly the carrying costs on a significant portion of the total outstanding long-term debt. While your Company's total debt burden is not insignificant, this re-structuring has had the effect of holding our cost of money at approximately 11% even in today's high cost money markets. Further re-structuring of presently outstanding debt is being actively pursued with a view to further reducing our cost of borrowed funds.

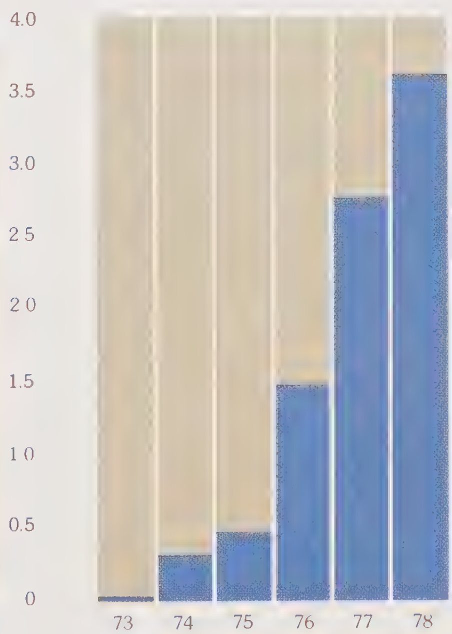
CRUDE OIL & NATURAL GAS SALES

(IN MILLIONS OF DOLLARS)



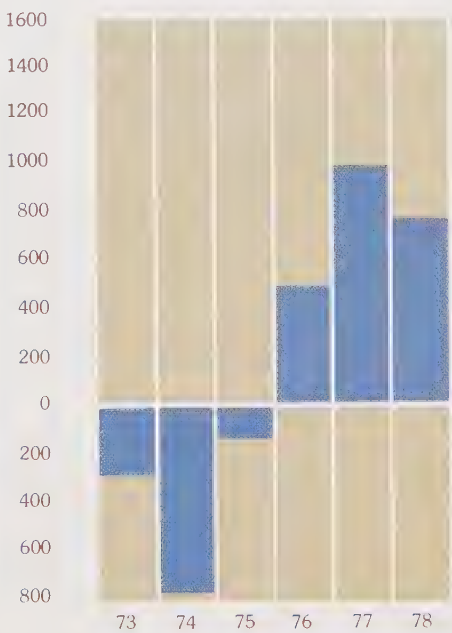
FUNDS PROVIDED FROM OPERATIONS

(IN MILLIONS OF DOLLARS)



ANNUAL NET INCOME

(IN THOUSANDS)



CONSOLIDATED BALANCE SHEET
AS AT DECEMBER 31, 1978

ASSETS	1978	1977
CURRENT ASSETS		
Cash	**$ 5,347,932**	$ 1,240,884
Accounts receivable — trade	**6,469,425**	2,596,491
— sale of property	**974,597**	3,700,000
	12,791,954	7,537,375
PROPERTY AND EQUIPMENT, at cost (note 2)	**53,310,525**	30,455,046
Accumulated depletion and depreciation	**10,310,487**	8,591,733
	43,000,038	21,863,313
OTHER ASSETS	**613,123**	160,920
	$56,405,115	$29,561,608

LIABILITIES		
CURRENT LIABILITIES		
Bank indebtedness (note 3)	**$ 1,530,113**	$ 2,936,153
Accounts payable and accrued liabilities	**7,752,980**	5,345,801
Income taxes payable	**70,475**	133,506
Current maturities on long-term debt	**372,500**	838,293
	9,726,068	9,253,753
LONG-TERM DEBT (note 3)	**36,077,589**	11,587,710
DEFERRED INCOME TAXES	**3,163,645**	2,076,018
MINORITY INTEREST	**775,572**	743,773

SHAREHOLDERS' EQUITY		
CAPITAL STOCK (note 4)		
Authorized		
1,000,000 Preferred shares without nominal or par value		
7,000,000 Common shares without par value		
Issued		
5,373,611 Common shares (1977 — 5,367,611)	**10,052,564**	10,029,474
CONTRIBUTED SURPLUS	**768,152**	768,152
	10,820,716	10,797,626
DEFICIT	**(3,473,840)**	(4,212,637)
	7,346,876	6,584,989
Less 595,334 Common shares held by wholly-owned subsidiary company	**(684,635)**	(684,635)
	6,662,241	5,900,354
	$56,405,115	$29,561,608

Approved by the Board

Director

Director

CONSOLIDATED STATEMENT OF EARNINGS
YEAR ENDED DECEMBER 31, 1978

	1978	1977
REVENUE		
Sale of oil and gas	$7,409,659	$5,434,977
Gain on sale of property	1,126,709	826,240
Interest and other	308,251	187,233
	8,844,619	6,448,450
EXPENSES		
Field operating	1,996,877	1,477,930
Non-producing property costs	158,086	106,062
Exploration, engineering and consulting	371,231	300,194
General and administrative	1,262,268	904,116
Interest on long-term debt	1,703,913	1,099,660
Other interest	238,937	—
Depreciation and depletion	1,763,323	1,340,143
	7,494,635	5,228,105
Earnings before income taxes and minority interest	1,349,984	1,220,345
Income taxes		
Provincial royalty tax credit	(421,127)	(256,012)
Current	50,580	57,737
Deferred	1,087,627	512,129
	717,080	313,854
Earnings before minority interest	632,904	906,491
Minority interest in consolidated company's losses	105,893	86,202
NET EARNINGS	$ 738,797	$ 992,693
EARNINGS PER SHARE	$ .15	$ .22

CONSOLIDATED STATEMENT OF DEFICIT
YEAR ENDED DECEMBER 31, 1978

	1978	1977
DEFICIT AT BEGINNING OF YEAR	$(4,212,637)	$(5,205,330)
Net earnings	738,797	992,693
DEFICIT AT END OF YEAR	$(3,473,840)	$(4,212,637)

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
YEAR ENDED DECEMBER 31, 1978

	1978	1977
WORKING CAPITAL DERIVED FROM		
Operations	**$ 3,651,948**	$ 2,781,958
Long-term debt	**39,273,171**	5,720,057
Issue of capital stock		
On conversion of 9% debenture	**—**	400,000
Pursuant to share purchase plan	**23,090**	—
Other	**19,400**	84,120
	42,967,609	8,986,135
WORKING CAPITAL APPLIED TO		
Acquisitions	**—**	984,338
Less working capital deficiency acquired	**—**	(686,001)
	—	1,670,339
Additions to property and equipment	**22,900,048**	7,547,316
Current maturities on long-term debt	**128,667**	635,398
Repayment of long-term debt	**14,654,625**	788,468
Other	**502,005**	92,531
	38,185,345	10,734,052
INCREASE (DECREASE) IN WORKING CAPITAL POSITION	**4,782,264**	(1,747,917)
WORKING CAPITAL (DEFICIENCY) AT BEGINNING OF YEAR	**(1,716,378)**	31,539
WORKING CAPITAL (DEFICIENCY) AT END OF YEAR	**$ 3,065,886**	$ (1,716,378)

AUDITORS' REPORT

To the Shareholders of
Oakwood Petroleums Ltd.

We have examined the consolidated balance sheet of Oakwood Petroleums Ltd. as at December 31, 1978 and the consolidated statements of earnings, deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1978 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Calgary, Canada
April 20, 1979

THORNE RIDDELL & CO.
Chartered Accountants

1. ACCOUNTING POLICIES

(a) Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly-owned, and American Eagle Petroleums Ltd. which was 44% owned at December 31, 1978. The Company has consolidated the accounts of American Eagle because management considers this to be the more informative presentation.

The excess of the consideration paid for shares of consolidated companies over the net book value of the assets acquired has been included in property and equipment in the consolidated balance sheet and is being amortized on the same basis as such assets, or has been deducted from shareholders' equity to the extent of the carrying value of the Company's shares held by the purchased company.

(b) Property and Equipment

The Company follows the practice of capitalizing the acquisition costs of both producing and non-producing properties and charging the costs to earnings if the property is subsequently surrendered. The cost of drilling a productive well is capitalized and the cost of a non-productive well is charged to earnings when the well is determined to be dry. The costs of producing leases and development thereon are amortized using the unit of production method based upon estimated quantities of oil and gas as determined by the Company's engineers.

All the Company's petroleum and natural gas exploration, development and production activities are conducted jointly with others. These consolidated financial statements reflect only the Company's proportionate interest in such activities.

Equipment is depreciated on a straight-line basis over its estimated useful life at annual rates varying from 10 to 20 percent.

(c) Income Taxes

The Company follows the tax allocation method of accounting under which the income tax provision is based on earnings reported in the financial statements. Accordingly, the Company makes full provision for income taxes deferred as a result of claiming capital cost allowances and exploration and development costs in excess of the amounts provided for depreciation and depletion in the financial statements. No deduction for income tax purposes is allowed for interest on the Company's income debentures (see note 3) which is included in interest on long-term debt expense in the consolidated statement of earnings.

(d) Foreign Currencies

The accounts of foreign subsidiaries have been translated into Canadian dollars on the following basis:

(i) current assets and liabilities at the rate of exchange at the end of the year;

(ii) all other assets, applicable depreciation and depletion and non-current liabilities at rates prevailing when the assets were acquired or the liabilities incurred;

(iii) revenue and expenses, except depreciation and depletion, at the average rate in effect during the year.

Gain or losses resulting from such translation practices are capitalized as part of property and equipment and subject to the same amortization policies (see note 1(b)).

(e) Deferred Charges

Financing charges related to the long-term debt have been deferred and are being amortized on a straight-line basis over the terms of the related debt.

2. PROPERTY AND EQUIPMENT

	1978			1977
	Cost	**Accumulated Depletion and Depreciation**	**Net**	Net
Producing petroleum and natural gas rights including development thereon	**$35,284,661**	**$ 8,248,410**	**$27,036,251**	$15,782,529
Production equipment	**9,230,808**	**1,964,341**	**7,266,467**	2,350,839
	44,515,469	**10,212,751**	**34,302,718**	18,133,368
Non-producing petroleum and natural gas rights including development thereon	**7,739,823**	**—**	**7,739,823**	3,452,884
Other property and equipment	**1,055,233**	**97,736**	**957,497**	277,061
	$53,310,525	**$10,310,487**	**$43,000,038**	$21,863,313

3. LONG-TERM DEBT

	1978	1977
Oakwood Petroleums Ltd. and subsidiaries		
Bank income debentures (a)	**$13,000,000**	$ —
Interim note (b)	**5,000,000**	—
Income debentures (c)	**5,000,000**	—
Production bank loans (d)	**10,428,828**	8,321,033
Prepayments under gas sales contracts	**382,066**	291,661
Fixed charge debentures	**—**	430,000
Notes payable	**—**	819,228
	33,810,894	9,861,922
Less current maturities included in current liabilities (f)	**112,500**	706,960
	33,698,394	9,154,962
American Eagle Petroleums Ltd. and subsidiaries		
Production bank loans (d)	**1,613,320**	1,400,000
Prepayments under gas sales contracts	**109,208**	164,081
Subordinated debenture (e)	**916,667**	1,000,000
	2,639,195	2,564,081
Less current maturities included in current liabilities (f)	**260,000**	131,333
	2,379,195	2,432,748
	$36,077,589	$11,587,710

(a) On November 15, 1978 the Company issued to a Canadian chartered bank $13 million of convertible income debentures maturing at various dates to January 1987 and bearing interest at one-half the prime rate set from time to time by the bank ("bank prime rate") plus 1¼%. The debenture which is secured by certain petroleum and natural gas properties is repayable in quarterly installments over six years commencing January 1981.

(b) On November 20, 1978 , the Company issued an interim note due February 26, 1979 bearing interest at bank prime rate plus 1%. The interim note was repaid on February 26, 1979 from the proceeds of a $20,000,000 term note due June 1, 1985 bearing interest at bank prime rate plus 1%. Both the interim and term notes are secured by specific interests in petroleum and natural gas properties and a floating charge on all other assets of the Company. The term note is repayable in monthly installments from April 1979 to June 1985.

(c) On October 15, 1978 the Company issued $5,000,000 of redeemable income debentures maturing October 15, 1993 and bearing interest at one-half bank prime rate plus 3%. The income debentures are secured by certain petroleum and natural gas properties of the Company and are redeemable in whole or in part after October 15, 1980. The holder may elect that the debentures mature in October 1983 or October 1988. Annual sinking fund payments of $400,000 are required from 1982 to 1992.

(d) The bank indebtedness included in current liabilities and production bank loans are evidenced by demand promissory notes and are secured by specific petroleum and natural gas properties, accounts receivable, and shares of American Eagle Petroleums Ltd. Interest is payable at the bank prime rate plus 1% to 1½%.

(e) The subordinated debenture is secured by a second floating charge on all assets of American Eagle. The debenture is repayable over five years by monthly installments which commenced August 1978. Interest is payable at the bank prime rate plus 1% (minimum 9% — maximum 12% per year).

(f) The production bank loans are repayable out of future production proceeds and, accordingly, are not expected to require the use of working capital; therefore, no portion of such loans has been reclassified to current liabilities. The estimated principal payments on long-term debt for the next five years are as follows: 1979 — $2,024,100; 1980 — $2,842,800; 1981 — $5,179,100; 1982 — $5,829,300; 1983 — $5,918,300.

4. CAPITAL STOCK

Changes in the Company's capital stock during the year ended December 31, 1978 were as follows:

	Number of Shares	Carrying Value
Balance at December 31, 1977	5,367,611	$10,029,474
Issued pursuant to share purchase plan	6,000	23,090
Balance at December 31, 1978	5,373,611	$10,052,564

Common shares have been reserved as follows:

	Number of Shares
For issuance to an officer at $4.17 per share pursuant to an option expiring March 14, 1981	100,000
For issuance pursuant to an employee stock option plan at prices varying from $3.83 to $4.05 per shares with expiry dates extending to September 7, 1983.	154,000
	254,000

Payment of dividends on common shares is subject to approval by the holders of certain of the Company's long-term debt.

5. SUBSEQUENT EVENT

Subsequent to December 31, 1978, the Company exercised its options to purchase, for approximately $19,200,000, interests in certain petroleum and natural gas properties. The funds for the acquisitions were provided from the proceeds of the $20,000,000 term note issued by the Company on February 26, 1979 (see note 3(b)) and production bank loans.

6. STATUTORY INFORMATION

During 1978 the consolidated group of companies paid $5,900 to the Company's nine directors in their capacity as directors and paid $355,769 to six officers of the Company, five of whom are also directors.

OAKWOOD

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